

2005

**SPECIAL ENROLLMENT
EXAMINATION**



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Part 1

SPECIAL ENROLLMENT EXAMINATION BOOKLET

**September 21, 2005
9:00 A.M. TO 12:00 NOON**

Individuals

Official Use Only
(Declassified After September 21, 2005)

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Special Enrollment Examination

Part 1

Individuals

Instructions:

Time allotted. You will have 3 hours to take the exam. No additional time will be given.

Source of questions. All references are to the Internal Revenue Code as amended through December 31, 2004. Unless otherwise stated, all questions relate to calendar year 2004.

Supplies provided. You will be given a No. 2 pencil, scratch paper, question booklet, and answer sheet. You may make computations on the scratch paper or question booklet and will turn these in with your test.

Contacting the monitor. Raise your hand to attract the monitor's attention if you need additional supplies or would like permission to leave the room.

Completing the answer sheet and making notes in the question booklet.

- Be sure to read each question carefully.
- Do not fold or tear the answer sheet since it will be machine graded.
- Use your No. 2 pencil to darken only one oval for each question.
- If you would like to make a correction, erase the error completely.
- You may want to also mark your answers in the question booklet because the booklet will be returned to you when your test has been graded. Your answer sheet will not be returned to you. The correct answers will be provided to you and you would then have the opportunity to compare your answers to the correct answers.

After you have finished.

- **Answer sheet.** You must turn in your answer sheet at the end of each test session or your test will not be graded. When you have finished the examination, you must turn in your answer sheet to the monitor before leaving the room.
- **Question booklet and scratch paper.** You must also turn in your question booklet and scratch paper (used and unused) before leaving the room. Any answers noted in your question booklet will not be graded. Your question booklet and scratch paper will be mailed to you after the examination has been administered in all sites.

Grading.

- **Point value of questions.** The questions in this examination have been assigned values of 1 to 3 points. All true or false questions have a value of 1 point each; the multiple choice questions in Section B have a value of 2 points each; and the multiple choice questions in Section C have a value of 3 points each.
- **Determination of correct answers.** The examination is graded on the basis of correct answers. If you darken more than one oval in answering a question, the answer will be considered incorrect.
- **Notification of results.** You will receive formal notification of your examination results on or about January 31, 2006.

Challenges. Challenges must be received by the Office of Professional Responsibility on or before October 22, 2005. Challenges must be on the form or in the format prescribed on www.irs.gov. Go to "tax professionals" and then to "enrolled agents".

Complete Personal Identifying Information: On your answer sheet in the space provided, you should enter the following information:

1. Print your name (First, M.I., Last).
2. Sign your name (First, M.I., Last).
3. Place of examination (City and State).
4. Date of this examination.
5. Print your name (Last, F.I., M.I.) in the boxes provided. Immediately below the boxes darken the oval corresponding to the letter you have printed, as in the sample Name Grid. Darken only one oval in each column below a box in which you have printed a letter. Make no marks in the columns below boxes you have left blank.
6. Enter your candidate number and immediately below, darken the oval corresponding to each number you have entered.
7. Enter your Social Security Number and immediately below, darken the oval corresponding to each number you have entered.

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Part 1
Section A:
Questions 1– 20

The following statements are either true or false. Select the most appropriate answer and darken the oval under A for True or B for False.

1. Kathy, a U. S citizen, is 22 and correctly files as single. In 2004, she had net self-employment income of \$550 after expenses. She had no other income or any tax payments. She does not have to file a federal income tax return for the year 2004.
2. If your spouse died during the year, you are considered married for the whole year for filing status purposes.
3. Tyler is single and is 18 years old. He works part time and is going to school. His total income for 2004 was \$8,000. Tyler lives with his parents. He qualifies as their dependent and they are claiming him as an exemption on their 2004 tax return. Since Tyler will file his own return, he may also take an exemption for himself.
4. Ted and Sharon (husband and wife) are the sole support of their 27-year-old son Tom who lives with them. Tom was unable to work in 2004 because of a medical condition but received \$3,500 from a charitable foundation for a speaking engagement. Ted and Sharon may claim Tom as a dependent on their 2004 federal income tax return.
5. Charles Moore had a \$2,000 tax liability in 2004. In 2005, Charles expects to owe at least \$1,500 in federal taxes. For 2005 he has no withheld income taxes. Charles does not need to file estimated taxes because his tax in 2005 is less than his 2004 tax.
6. Dianne deposited \$10,000 in a bank to purchase a 6 month money market certificate which matures in 2004. The bank gave her a Form 1099-INT for 2004 showing the \$575 interest earned. Dianne is required to include this interest as income for tax year 2004.
7. John frequently pays for repairs in his apartment and gives the receipts to his landlord in lieu of part of his rental payment. The landlord is entitled to deduct the repair expenses (non-capital improvements) on his tax return but must also report these amounts as rental income.
8. Denise worked for 3 months in Russia and earned foreign income. Denise is a United States citizen and, except for the 3 months spent in Russia, resides in Mobile, Alabama. Denise did not receive either a Form W-2 or a Form 1099 for her earnings while in Russia. Because Denise resides in the U.S., is a U.S. Citizen, and did not receive any tax reporting forms, she does not have to report any of the income she earned in Russia.
9. Mary, a single woman, bought her home in June 2001 for \$350,000. She lived in the house until she sold it in July 2004 for \$600,000. Mary is able to exclude the maximum amount of gain from the sale of her home.
10. You may be able to exclude your gain from the sale of a home that you have used for the use of a business if you meet the ownership and use tests. You may be entitled to take depreciation deductions because you used your home for business purposes. However, you can not exclude the part of your gain equal to any depreciation allowed as a deduction for periods after May 6, 1997.
11. In 1995, John and Kim Jones (husband and wife), bought their primary residence for \$250,000. In 2004 they sold it for \$550,000, taking the maximum allowable exclusion. They are not required to report the sale of their home on their tax return.
12. Sonja is a calendar-year taxpayer. A flood damaged her home on June 2004. The flood damaged or destroyed a considerable amount of property in her town. The President declared the area that includes Sonja's town a federal disaster area as a result of the flood. Sonja can choose to deduct the flood loss on her home on last year's tax return.
13. The eligibility rules for Earned Income Tax Credit only apply to single parent households.
14. The rules of a university state that an individual can become a faculty member only if he or she achieves an advanced or graduate degree. University rules also state that an individual, hired as a temporary instructor without an advanced or graduate degree, can keep his or her instructing job only as long as he or she shows satisfactory progress toward achievement of this advanced or graduate degree. Mike has a bachelor's degree and was previously hired as a temporary instructor at this university. Mike is taking graduate courses toward his advanced degree, but has not met the minimum educational requirements to qualify as a faculty member. Mike's graduate courses are **not** considered to be qualifying work-related education.
15. Ron sold property for \$10,000. The agreement calls for \$1,000 as a down payment and \$1,500 in each of the next 6 years to be made from an irrevocable escrow account. The escrow account contains funds provided by the purchaser for the balance of the purchase price plus interest. Ron can use the installment method to report the sale.
16. You may be able to take a credit against your regular tax in the current year for alternative minimum tax liability paid in a prior year.

17. You cannot take a credit (or deduction) for foreign income taxes paid on income that you exclude from U.S. tax under the foreign earned income exclusion.
18. Scott and Kathy's (husband and wife) son turned 17 years of age on December 30, 2004. Scott and Kathy claimed their son as a dependent on their return for 2004. Scott and Kathy's son is also considered as a qualifying child for the child tax credit.
19. James is 28 years old, single and has no children. He lives at home with his parents. He works as a part-time truck driver. His income for 2004 was \$6,050. He also has interest income of \$200 from a savings account. James is entitled to \$390 earned income credit for 2004.
20. The tax law gives special treatment to certain types of income and allows special deductions and credits for certain types of expenses. Taxpayers who benefit from the law in these ways may have to calculate the alternative minimum tax (AMT). In the initial year of assessment, the AMT is a tax credit against your regular tax.

Turn to the next page for Part 1, Section B.

Part 1
Section B:
Questions 21 - 45

The following questions are multiple choice. Select the most appropriate answer and darken the oval under the corresponding letter on the answer sheet.

21. Matt has a certified statement from his optometrist on December 1, 2004, that confirms he can see no better than 20/250. For tax year 2004, which is correct?
- A. Matt is not eligible for the higher standard deduction for blindness as he is only partially blind
 - B. Matt is eligible for the higher standard deduction for blindness in 2004
 - C. Matt is eligible for the higher standard deduction for blindness in 2005, the first full year of his blindness
 - D. Matt is not eligible for the higher standard deduction for blindness as he can see better than 20/300
22. Which of the following statements is true regarding the filing of a Form 4868, Application for an Automatic Extension of Time to File, your 2004 tax return?
- A. Interest is not assessed on any income tax due if a Form 4868 is filed
 - B. Form 4868 provides the taxpayer with an automatic additional 6 month extension to file
 - C. Even though you file Form 4868, you will owe interest and may be charged a late payment penalty on the amount you owe if you do not pay the tax due by the regular due date
 - D. A U.S. citizen, who is out of the country on April 15, will be allowed an addition 12 months to file as long as "Out of the Country" is written across the top of Form 4868
23. Lisa was married with two dependent children in 2004. Her husband died in April and she did not remarry before the end of 2004. Which filing status should Lisa use for her tax return in 2004?
- A. Single
 - B. Married Filing Jointly
 - C. Head of Household
 - D. Qualifying Widow(er) With Dependent Child
24. There are five tests which must be met for you to claim an exemption for a dependent. Which of the following is **not** a requirement?
- A. Citizen or Resident Test
 - B. Member of Household or Relationship Test
 - C. Disability Test
 - D. Joint Return Test
25. Which statement pertaining to estimated tax payments is not correct?
- A. An individual, whose only income is from self-employment, will have to pay estimated payments
 - B. If insufficient tax is paid through withholding, estimated payments may be necessary
 - C. Estimated tax payments are required when the withholding taxes are greater than the overall tax liability
 - D. Estimated tax is used to pay not only income tax, but self-employment tax and alternative minimum tax as well
26. Mrs. Domino made deductible contributions to traditional individual retirement accounts for several years. Mrs. Domino decides to withdraw \$10,000 from one of her accounts in 2004. Mrs. Domino is 61 years old. How does this transaction affect Mrs. Domino's 2004 tax return for 2004?
- A. Mrs. Domino must report the entire amount of \$10,000
 - B. Mrs. Domino does not have to report anything because she is older than 59½ years
 - C. Mrs. Domino does not have to report any amount because this was not withdrawn from a Roth IRA
 - D. Mrs. Domino must report all of the distribution received but can elect to use the 10-year option
27. Randy Lee is an ordained minister of a tax-exempt church. Randy receives a salary plus a housing allowance for rent and utilities. Which of the following statements is correct?
- A. Randy must claim as income on his return all of his salary and all of his housing allowance. The salary is subject to income tax and self-employment tax but his housing allowance is subject to income tax only
 - B. Randy does not have to report any income received from the church because the church is tax exempt
 - C. Randy has to pay both income tax and self-employment tax on his salary, but only self-employment tax for the housing allowance. The housing allowance is not subject to income tax
 - D. Randy only has to pay the self-employment tax on both his salary and the housing allowance. Neither is subject to income tax
28. Tom Brown, who is single, owns a rental apartment building property. This is the only rental property that Tom owns. He "actively participates" in this rental activity as he collects the rents and performs ordinary and necessary repairs. In 2004, Tom had a loss of \$30,000 on this rental activity and had no reportable passive income. His adjusted gross income, without regard to this rental loss, is \$60,000. How much of the rental loss may Tom deduct on his 2004 return?
- A. \$30,000
 - B. \$25,000
 - C. \$0
 - D. \$6,000

29. Which of the following costs incurred on rental property should be classified as a capital improvement?
- Replacing a 20-year-old roof
 - Repainting all of the interior walls
 - Refinishing the existing wood floors
 - Replacing a broken window pane
30. The Becks own and operate an assisted-living facility. They provide maid service and meals in a common dining room. Where should they report the income and expenses from this activity?
- Other Income on Form 1040 and expenses as itemized deductions on Schedule A
 - Income and expenses on Schedule E, Supplemental Income and Loss
 - Income and expenses on Schedule C, Profit or Loss from Business
 - Short-term capital gain on Schedule D
31. In January of 2004, Mrs. Black purchased an office building and used office furnishings. The used office furnishings consisted of chairs, desks, and file cabinets. \$900,000 of the purchase price was allocated to the office building and \$50,000 of the purchase price was allocated to the used office furnishings. According to the General Depreciation System (GDS) under MACRS for depreciation, what recovery period must she use for the purchased items?
- 27.5 years for the entire asset, building and furnishings
 - 39 years for the building and 5 years for the used office furnishings
 - 27.5 years for the building and 7 years for the used office furnishings
 - 39 years for the building and 7 years for the used office furnishings
32. Jan owns and operates a store in the downtown shopping mall. She reports her income and expenses as a sole proprietor on a Schedule C. In 2004 one of the financial institutions that she borrowed money from in order to start her business cancels her debt. Jan had a balance due of \$5,000 when the debt was canceled. Which of the following statements is true?
- Jan does not have to report the forgiveness of the debt as income
 - Jan must report the \$5,000 debt cancellation as other income on Form 1040
 - Jan has to report the \$5,000 debt cancellation as income on her Schedule C
 - Jan has to report the relief of debt of \$5,000 as a long-term gain on Schedule D
33. Juan purchased two shares of common stocks in 2004 in a company that markets biotech products. Juan paid \$90 for one share and paid \$110 for the next share. Later that year, the company declared a 2 for 1 common stock split. Juan's new basis in the stock shares is:
- Average of the 4 shares at \$50 a share
 - Two shares at \$90 a share and two shares at \$110 a share
 - Four shares at \$200 a share
 - Two shares at \$45 a share and two shares at \$55 a share
34. In computing the gain or loss from a sale or trade of property, which statement below best describes the amount you realize?
- The money you actually receive
 - The fair market value of the property on the transaction date
 - Everything you receive for the property
 - The value of any services you received
35. John bought his principal residence for \$250,000 on May 3, 2003. He sold it on May 3, 2004, for \$400,000. What is the amount and character of his gain?
- Long-term, ordinary gain of \$650,000
 - Long-term, capital gain of \$150,000
 - Short-term, ordinary gain of \$650,000
 - Short-term, capital gain of \$150,000
36. Joe had a taxable gain on the sale of his main home, which could not be excluded on his 2004 tax return. He had no business use of the home. Which schedule does he need to submit to report the gain?
- Schedule C, for sole proprietors
 - Schedule A, for itemized deductions
 - Schedule D, for capital gains
 - Schedule SE, for self-employment income
37. Shannon and Dan Smith (wife and husband) purchased Section 1244 (Small Business) stock in 2004. Which of the following statements is correct?
- If they incurred a loss on Section 1244 stock, they can deduct the loss as a capital loss rather than as an ordinary loss
 - If the stock becomes worthless, they can claim an ordinary loss limited to \$50,000 individually or \$100,000 together on a joint return, per year
 - If the loss is \$60,000 and Shannon does not have any other losses, Dan can only deduct \$50,000 as ordinary loss on the joint return
 - If they incurred a gain on Section 1244 stock, they should treat it as ordinary gain
38. Megan, an engineer, maintains a residence for herself in Phoenix, Arizona where her employer maintains a satellite office. In 2004 Megan's employer enrolls her in a 12-month executive training program at their corporate offices in Santa Clara, California. Megan will attend classroom training in Santa Clara and temporary work assignments throughout the United States, but does not expect to expect to return to work in Phoenix after she completes her training. Every Monday morning she takes a commuter flight to Santa Clara. She maintains a small, one bedroom apartment in Santa Clara and incurs all the ordinary and necessary expense in the upkeep of a home. Her grandparents live in a separate residence in Phoenix, so she returns to Arizona on weekends to spend time with them and also attend to her personal affairs from her Phoenix residence. Where can Megan consider her "tax home" to be for the year 2004?
- Santa Clara, California
 - Phoenix, Arizona
 - Neither because Megan is a transient
 - Both because Megan spends time in both places

39. Marco and Leigh Ann Green (husband and wife) moved from New Jersey to Florida on May 1, 2004, at Marco's request. Leigh Ann immediately found a job as a part time substitute teacher, but only worked 23 weeks during the year. Marco, a self-employed solar heating unit salesman, could not continue in the same line of work after the move. In Florida he held one full-time job for 10 weeks, then another full time job for 6 more weeks during 2004. Marco expects that he will start a new full-time job as an employee of a landscaping company in January of 2005. Can Marco and Leigh Ann claim a deduction for moving expenses on their 2004 jointly filed return?
- They cannot, since Marco did not meet the 39 week test in 2004
 - They can, since Leigh Ann worked 23 weeks and Marco worked 16 weeks for a total of 39 weeks
 - They can, since Marco expects to meet the 39 week test in 2005
 - They cannot, since both Leigh Ann and Marco have to meet the 39 weeks test individually
40. Which of the following expenses are **not** deductible as medical expenses?
- Insulin used for diabetes
 - Wig, purchased upon the advice of a physician for the mental health of a patient who has lost all of his/her hair from disease
 - Swimming lessons, recommended by a doctor for improvement of general health
 - Acupuncture used for migraines
41. Rosa purchased a home in Quogue, NY in 1990 but she lives in Brooklyn with her sister. She lets her son Bob and his wife Samantha live in the Quogue house. Astoria Bank holds the mortgage with only Rosa's name on the property as she did not add her son's name to the property deed. Since Bob lives in the Quogue house, he makes the monthly mortgage payments to Astoria Bank. Who can deduct the mortgage interest expense for the year 2004?
- Bob, since he makes the payments
 - Rosa, since she owns the property and is liable for the payments
 - Both, since they are related
 - Neither, since Rosa is not paying her liability and Bob is paying for what he is not liable
42. Vera and Jack (wife and husband) contributed \$15,000 in cash to their synagogue during 2004. They also donated \$3,000 to a private foundation which is a non-profit cemetery organization. They knew a 30% limit applies to contributions to such foundations. Their adjusted gross income for the year 2004 was \$30,000. Vera and Jacks' deductible contribution for the year 2004 and any carryover to next year is:
- \$18,000 with \$0 carryover to next year
 - \$15,000 with \$2,100 carryover to next year
 - \$7,500 with \$2,100 carryover to next year
 - \$15,000 with \$3,000 carryover to next year
43. Julie made cash contributions to her local chapter of the Society for Prevention of Cruelty to Animals (SPCA) to care for stray dogs and cats. She donated several times a year but she paid less than \$250 for the entire year. These are the only charitable contributions Julie makes during the year. What documentation must Julie keep and provide to the Internal Revenue Service upon request in order to substantiate her tax return charitable contribution deduction?
- No documentation is necessary since the contribution is less than \$250
 - A receipt for each donation that shows the amount, date, and to whom paid
 - An acknowledgement from the SPCA that she made contributions during the year
 - A self-prepared statement or letter would be sufficient for contributions less than \$250
44. Which of the following items is not tax deductible as an education related expense?
- Certain transportation and travel costs
 - The dollar value of vacation time or annual leave you take to attend a class
 - Tuition, books, supplies, lab fees, and similar items
 - Costs of research and typing when writing a paper as part of an educational program
45. Which of the following is **not** a requirement for a qualifying child for purposes of the Child Tax Credit?
- The child is claimed as your dependent
 - The child was under age 19 at the end of 2004 or under age 24 at the end of 2004 and was a student
 - The child is your son, daughter, adopted child, grandchild, stepchild, or foster child
 - The child is a citizen or resident of the United States

Turn to the next page for Part 1, Section C.

Part 1
Section C:
Questions 46 - 80

The following questions may require some computation. Select the most appropriate answer and darken completely the oval under the corresponding letter on the answer sheet.

46. Kiran bought stock in the Big Bang Corporation in 1999 for \$2,000. In 2003, Kiran received a return of capital distribution of \$100 as a partial return on her investment. In 2004 Kiran sold the stock for \$3,000. Her basis in the stock is:

- A. \$3,000
- B. \$2,100
- C. \$1,900
- D. \$2,000

47. Kathy rented out her summer home for 80 days plus used it personally for 20 days. She paid \$1,000 for repairs and \$2,000 for utilities. Rental income was \$8,000. What was Kathy's net rental income?

- A. \$0
- B. \$5,000
- C. \$5,600
- D. \$8,000

48. Ms. Cross owns a house that she rents to non-related parties. She incurred the following costs during 2004:

- \$400 to resurface a tub in the master bathroom.
- \$500 to paint the kitchen after installing new cabinets.
- \$2,000 to replace cabinets in the kitchen.
- \$600 to replace the built-in dishwasher.

How should these costs be characterized and in what amounts?

- A. \$3,100 as improvements to be capitalized and \$400 as repairs
- B. \$400 as improvements to be capitalized and \$3,100 as repairs
- C. \$3,500 as improvements to be capitalized
- D. \$2,000 as improvements to be capitalized and \$1,500 as repairs

49. Joan received a scholarship for purposes of attending the University of California at Los Angeles. Joan is not a degree candidate. The scholarship consisted of \$6,000 for tuition, \$1,500 for fees, \$500 for books, \$800 for required equipment, and \$6,000 for room and board. Which of the following amounts should Joan include in her taxable income?

- A. \$6,000
- B. \$14,800
- C. \$0
- D. \$6,800

50. Mr. and Mrs. Clark are both 72 years of age, married, filing jointly. They received social security benefits of \$7,500 each. Additional income is a taxable pension of \$12,000 for Mr. Clark and \$6,000 for Mrs. Clark. What is the taxable portion of the social security benefits received by the Clarks?

- A. \$15,000
- B. \$7,500
- C. \$3,750
- D. \$0

51. Ed purchased a house on an acre of land from Ruth on June 30, 2004. Prior to the purchase Ed had been renting the house from Ruth for \$500 per month. Ed paid the following amounts:

- \$100,000 in loan proceeds to Ruth
- \$2,000 in points to the bank
- \$1,000 in real estate taxes Ruth owed to the town
- \$1,000 in past due rent to Ruth
- \$1,000 in closing costs to the bank for legal, recording, title insurance and survey fees
- \$1,000 in escrowed Real Estate taxes to the bank

What is Ed's basis in the house and land purchased from Ruth?

- A. \$100,000
- B. \$102,000
- C. \$104,000
- D. \$106,000

52. In 2004, Tran received a vacant parcel of land from her uncle as a gift. Tran's uncle purchased the land in 1990 for \$15,000, and at the time of the gift to his niece, he paid \$500 in gift tax based on the land's fair market value of \$13,000. Tran did not have any other events that increased or decreased her basis in the gift after she received it. What is her gain if she sold her property for \$17,000?

- A. \$4,000 gain
- B. \$3,500 gain
- C. \$2,000 gain
- D. \$1,500 gain

53. Richard collected baseball cards as a hobby. Richard had shared his interest in this hobby with his niece Susan, who was now also an avid card collector. At the time of his death in 2004 Richard's collection had a fair market value of \$10,000 and an adjusted basis of \$2,000, while Susan's collection had a fair market value of \$5,000 and an adjusted basis of \$1,000. Upon his death Richard's entire card collection went to Susan. With the death of her uncle, Susan lost interest in the hobby and sold all of the cards for \$20,000. What is Susan's gain on the sale of these baseball cards?

- A. \$5,000
- B. \$9,000
- C. \$13,000
- D. \$17,000

54. In 2002 Mary purchased 10 shares of Acorn Corporation common stock for \$100 per share. In 2003 Mary purchased an additional 10 shares of Acorn Corporation common stock for \$200 per share. At the end of 2004, Acorn Corporation declared a 2 for 1 common stock split. What is Mary's total basis in her Acorn Corporation common stock?
- \$300
 - \$400
 - \$500
 - \$600
55. Joe exchanged a building for another like-kind building. Joe had a basis of \$16,000, plus he had made \$10,000 in improvements prior to the exchange. He exchanged it for a building worth \$36,000. Joe did not recognize any gain from the exchange on his 2004 individual tax return. What is Joe's basis in the new property?
- \$26,000
 - \$36,000
 - \$10,000
 - \$16,000
56. John is a furniture maker and carpenter. John makes half of his income as an employee of Concept Designs, Inc., a fine furniture manufacturing corporation. John makes the other half of his income from a personal business where he purchases, renovates and then resells houses. In January of 2004 John purchases a house that is not his residence for \$50,000. He spends \$10,000 in materials renovating the house, which he sells in November of 2004 for \$90,000. What is the amount and character of John's gain from this transaction?
- \$20,000 ordinary gain
 - \$30,000 short-term capital gain
 - \$30,000 ordinary gain
 - \$20,000 short-term capital gain
57. Alf owns all of the shares of Waxman Corporation, a manufacturer of finished leather products. Alf also owns a 60% partnership interest and his friend Richard owns a 40% partnership interest in York Real Estate Rentals, LLC. York Real Estate Rentals, LLC owns and leases warehouse space to numerous businesses. In 2004, York Real Estate Rentals, LLC sold a building with an adjusted basis of \$100,000 to Waxman Corporation for \$80,000. What is the amount of York Real Estate Rentals, LLC's deductible loss in 2004 from this transaction?
- \$(20,000)
 - \$(12,000)
 - \$(8,000)
 - \$(0)
58. Yang and May Ling (husband and wife) owned a fashionable handbag store in New York, which they report as a sole proprietorship on their individual return. They had the following types of transactions during the 2004 year:
- \$600,000 from the sale of a rare coin collection May Ling inherited in February of 2003.
 - \$100,000 received in accounts receivable from sales of 500 bags in November of 2004.
 - \$50,000 from sale of stocks held in their personal account that were purchased in 2002.
 - \$5,000 for the purchase of supplies such as computer paper, invoices, etc used in the business.
- From the information provided, what is the proper gross amount and characterization of capital transactions that Yang and May Ling should report for the year 2004?
- \$650,000 as long-term capital gain
 - \$695,000 as ordinary income
 - \$50,000 as long-term capital gain
 - \$95,000 as short-term capital gain
59. Yasmin purchased 50 shares of Tele Company stock on February 6, 2004, at \$20 a share. She sold all 50 shares on February 23, 2004, for \$15 a share. Later on the same day, she repurchased 40 shares of Tele Company stock at \$16 per share. With only the information provided, what is Yasmin's net capital loss that she can deduct on her 2004 return?
- \$250 net capital loss
 - \$640 net capital loss
 - \$750 net capital loss
 - \$0 net capital loss, but she can add \$250 to her new stock basis
60. Yousef and Ramina (husband and wife) purchased 10 shares of stocks in Yam Company on August 31, 2003, for \$850. They sold 25 shares of stock in Tray Company for \$900 on April 10, 2004. They had purchased the 25 Tray Company shares in 1993 for \$100. They also sold 20 shares of stock of Delta Company on December 1, 2004 for \$500. They had purchased the 20 Delta Company shares in 2002 for \$4,500. Yousef and Ramina's taxable income on their joint 2004 return was \$33,000 before these stock transactions. Assume Yousef and Ramina had no other capital transactions in 2004. What is Yousef and Ramina's currently deductible capital loss for 2004 and what is their capital loss carryover to the next year?
- They can deduct \$3,200 in long-term capital loss and carry over a capital loss of \$800
 - They can deduct \$4,000 in long-term capital loss
 - They can deduct \$3,000 in long-term capital loss and carry over a capital loss of \$200
 - They can deduct \$500 in long-term capital loss

61. Ernest, a self-employed watch maker, traveled to Germany in September of 2004. During his five day stay in Germany he attended a 2 hour watch making seminar in the city of Berlin on a Monday and took a 4 hour tour of a watch manufacturing facility in Dresden on a Wednesday. The rest of the time Ernest spent hiking and touring the countryside. Ernest incurred the following costs for this trip:
- Round trip airfare of \$500
 - Lodging of \$1,000
 - Meals of \$300
 - Seminar and tour registration fees of \$200
- In 2004, what is the amount that Ernest can deduct for travel, meals and entertainment for this trip to Germany?
- \$2,000
 - \$800
 - \$200
 - \$0
62. Sam owns a plumbing supply business that he reports as a sole proprietorship. Sam spends a great deal of time and money entertaining clients. A lot of Sam's business is conducted in restaurants and on the golf course. In 2004 Sam incurred the following expenses:
- \$2,000 in meal expenditures for client business dinners
 - \$300 in babysitting fees during client business dinners
 - \$1,000 in golf club membership dues
 - \$200 in golf equipment
- In 2004, what is the amount that Sam can deduct for business entertainment expense?
- \$3,000
 - \$2,000
 - \$1,500
 - \$1,000
63. Cindy is a sales person employed by a window manufacturing company and she travels to various locations to sell her products. She drives 12,000 miles a year. She adequately accounts to her employer for her business expenses. Her employer reimburses her \$3,600 for the mileage driven at 30 cents a mile. Based on the standard mileage rate of 37.5 cents a mile, her expense was \$4,500. Cindy is entitled to deduct on Schedule A, Itemized Deductions, transportation expenses of:
- \$0 since Cindy was reimbursed by her employer
 - \$900 as excess expense over the reimbursed expense
 - \$3,600 since she was reimbursed for that amount
 - \$4,500 since she can claim the standard mileage rate
64. Starting in 2004, Mr. West must pay his former spouse \$20,000 annually under a divorce decree in the following amounts:
- \$1,000 a month for mortgage payments (including principle and interest) on a jointly owned home
 - \$200 a month for tuition fees paid to a private school until their son attains the age of 18 or leaves the school prior to age 18
 - \$5,000 a year cash payment to former Mrs. West
 - In addition to the above amounts, the former Mrs. West also received in 2004 a lump-sum amount of \$150,000 from the sale of their other marital assets.
- Assume the parties did not file a joint return and were not members of the same household. Also, assume that there were no written statements between the parties as to how the amounts should be treated. What is the amount of Mr. West's 2004 alimony deductions?
- \$20,000
 - \$155,000
 - \$17,600
 - \$11,000
65. Mr. Green must use a wheelchair. Upon advice from his doctor, in 2004 he installed an elevator and widened the front entrance of his house, incurring \$10,000 and \$3,000 in respective costs. Mr. Green had purchased his house for \$146,000. An appraisal showed the fair market value of Mr. Green's house immediately after these modifications at \$154,000. Also in 2004 Mr. Green decided to join a health club primarily to improve business contacts and for recreational purposes. He paid a \$1,250 annual membership fee to make use of this facility.
- Compute Mr. Green's currently deductible medical expense.
- \$14,250
 - \$5,000
 - \$13,000
 - \$6,250
66. Mr. and Mrs. Mead, both full time teachers, wanted to volunteer their services to work for the tsunami victims. Their services consisted of going to various neighborhoods in the community to raise funds for the tsunami cause. While volunteering the Mead's kept records of the costs involved. These costs included time spent, out of pocket expenses for travel, and car expenses.
- The Mead's valued their volunteered time at \$500 total for the year,
 - Out of pocket expenses that were directly related to their services rendered at \$25 for parking fees and \$350 for gas and oil, and
 - Car expenses for new tires at \$200 and registration fees at \$90.
- If the Mead's elect to take the actual expenses, in 2004 how much can they deduct?
- \$375
 - \$665
 - \$875
 - \$1,165

67. Alberta and Archie (wife and husband) had water damage in their home during 2004 which ruined the furniture in their basement. The following items were completely destroyed and not salvageable.

Damaged Items:	Fair market value just prior to damage:	Original item cost:
Antique bed frame	\$5,000	\$4,000
Pool table	\$8,000	\$10,000
Large screen TV	\$700	\$2,500

Their homeowner's insurance policy had a \$10,000 deductible for the personal property, which was deducted from their insurance reimbursement of \$12,700. Their adjusted gross income for 2004 was \$30,000. What is the amount of casualty loss that Alberta and Archie can claim on their joint return for 2004?

- A. \$10,600
B. \$3,400
C. \$6,900
D. \$0
68. The state condemned Joe's property. Joe did not hold the property for use in a trade or business or for investment. The adjusted basis of the property was \$26,000. The state paid Joe \$36,000 in 2004. Joe realized a gain of \$10,000. Joe bought like-kind property for \$35,000 in 2004 for the purpose of replacing the condemned property. Joe also made a proper Internal Revenue Code section 1033 election to defer gain from the condemnation on his 2004 tax return. In 2004, what is the net taxable gain and where must Joe report it?
- A. \$36,000 on the return Schedule D
B. \$10,000 on line 21 of the Form 1040
C. \$1,000 on Schedule D
D. \$26,000 on Form 4797 – Sale of Business Property
69. Bethany and Michael (wife and husband) are itemizing their Schedule A expenses on their tax year 2004 return. Michael traveled to Japan for his employer, but was not reimbursed. His meal expenses totaled \$500. How much can Michael deduct for meals prior to the 2% limitation?
- A. \$250
B. \$500
C. \$150
D. \$0

70. Jack had the following income in 2004:

- \$59,800 in wages
- \$200 in interest
- \$10,000 in gambling winnings
- \$5,000 in short-term capital gains.

Jack filed a Schedule A, Itemized Deductions, for 2004. While preparing that schedule, Jack listed the following deduction items he had incurred during the year:

- \$2,500 in medical expenses
- \$8,000 of mortgage interest paid
- \$2,000 in real estate taxes
- \$1,600 in state taxes
- \$12,000 in gambling losses
- \$3,400 in employee business expenses.

What is the total amount of Schedule A itemized deductions that Jack can report in 2004?

- A. \$27,500
B. \$25,000
C. \$23,500
D. \$20,100
71. Laurie is a sophomore in the University of Nebraska's degree program in dentistry. In 2004, Laurie paid \$3,000 in tuition, \$500 for books, and \$250 for rented dental equipment. Laurie also paid room and board of \$3,500. What is the total qualifying educational expense for Laurie in 2004?
- A. \$3,500
B. \$3,750
C. \$7,250
D. \$3,000
72. Bob and Naomi (husband and wife) sold their boat for \$75,000 with a gross profit of \$25,000. What is Bob and Naomi's gross profit percentage for this sale?
- A. 25 %
B. 33 1/3 %
C. 30 %
D. 3 %
73. Thomas loaned friend Susan \$10,000 for a down payment on a home. Thomas and Susan signed a note in which Susan agreed to pay \$100 a month with an interest rate of 4% until the loan was completely paid. Susan lost both her job and her home in 2003. Susan filed bankruptcy and went to live with her mother. Thomas sued Susan in court for non-payment in August 2004, but the court dissolved her debt to Thomas based upon the bankruptcy. When Susan defaulted, the outstanding balance due on the note was \$7,000. If Thomas had only wage income reportable during the year, how much would his deductible bad debt be in 2004?
- A. \$7,000
B. \$6,900
C. \$3,000
D. \$10,000

74. Cecilia, employed as a nurse, incurred the following expenses during 2004.

- \$2,000 in attorney fees related to the collection of alimony payments
- \$8,000 in gambling losses
- \$1,000 in uniform purchase costs
- \$900 in union dues

Cecilia also had stereo equipment valued at \$3,000 stolen from her home in 2004. Cecilia's adjusted gross income (AGI) for 2004 was \$90,000, included in which were gambling winnings of \$2,000. For 2004, what is the amount of miscellaneous itemized deductions subject to the 2% of AGI limitation that Cecilia can report after deducting the 2% of AGI limitation?

- A. \$8,900
- B. \$2,100
- C. \$5,900
- D. \$3,100

75. Raul and Monika (husband and wife) are both lawyers and they contribute money to various organizations each year. They file a joint return and their adjusted gross income for 2004 is \$100,000. They contributed to the following organizations in 2004:

- \$5,000 to Alta Sierra country club
- \$10,000 to prevent cruelty to animals
- \$2,000 to State Bar association (This state bar association is not a political subdivision of the state, serves both public and private purposes, and the funds uses are unrestricted and can be for private purpose.)
- \$12,000 to cancer research foundation
- Donated clothing to Salvation Army. (Raul purchased the items for \$1,000, but the fair market value of the same items at a thrift store is equal to \$50.)

How much can Raul and Monika deduct as charitable contributions for the year 2004?

- A. \$29,050
- B. \$25,000
- C. \$22,050
- D. \$24,000

76. Samuel, a civil engineer, drives his own vehicle to various locations to inspect bridges for safety standard requirements. His employer reimburses Samuel \$400 each month for various business expenses and does not expect Samuel to provide proof of his expenses. His employer included this \$4,800 reimbursement in Samuel's 2004 W-2 as part of his wages. In 2004, Samuel incurred \$3,000 in transportation expense, \$1,000 in parking and tolls expense, \$1,800 in car repairs expense, and \$600 for expenses while attending a professional association convention. Assume Samuel uses the vehicle for business purposes only and that he maintains adequate documentation to support all of his above expenditures.

What amount is Samuel entitled to deduct on his Schedule A for Itemized Deductions?

- A. \$6,400 of expenses subject to the 2% of adjusted gross income limitation
- B. \$1,600, the difference between his expenditures and what he was reimbursed
- C. \$0 since his employer follows non-accountable plan
- D. \$4,800 since his employer follows non-accountable plan

77. Mark owned 100% of the stock in Gathers Corporation. In 2004, Gathers Corporation sold a computer with an adjusted basis of \$5,000 and a fair market value of \$8,000 to Mark's Uncle Seth for \$4,000. What is the amount of Gathers Corporation deductible loss on the sale of this computer in 2004?

- A. \$(4,000)
- B. \$(3,000)
- C. \$(1,000)
- D. \$(0)

78. Wanda purchased a manuscript in 1923 for \$10. In 2002, the year before her death, Wanda gave the manuscript to her granddaughter Ruth. At the time of the gift the manuscript had an appraised value of \$510. In 2004 Ruth sells the manuscript for \$1,010. What is the amount and character of Ruth's gain from the sale of this manuscript?

- A. \$1,000 long-term capital gain
- B. \$1,000 ordinary gain
- C. \$500 long term-capital gain
- D. \$500 ordinary gain

- 79.** In 2002 Fred purchased 100 shares of Oak Company common stock for \$100 per share. In June of 2004, Oak Company declared a 2 for 1 common stock split. Fred sells 50% of his Oak Company common stock shares for \$200 per share immediately after he receives his stock split shares. He sells his remaining Oak Company shares at the end of 2004 for \$100 per share. What is Fred's total 2004 gain from the sale of his Oak Company shares?
- A. \$15,000
 - B. \$20,000
 - C. \$25,000
 - D. \$30,000
- 80.** In 2003, Tony received a gift of 200 shares of mutual funds stock. The stock was worth \$20,000 when Tony received it. The donor had originally paid \$10,000 for the stock when he bought it in 1999. Tony sold the stock for \$15,000 in 2004. What is Tony's basis in the stock, disregarding gift tax?
- A. \$0
 - B. \$20,000
 - C. \$10,000
 - D. \$15,000

End of Part 1.